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No. 82-903

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1982

EMI LIMITED,
Plaintiff, Appellant and Petitioner,

VS.

WILLIAM BENNETT, KENNETH CORY, MARY ANN GRAVES, AND GERALD H. GOLDBERG,
Defendants and Respondents.

On Petition for Writ of Certiorari To the United States Court of Appeals for the Ninth Circuit Prior to Entry of Decision in That Court and While Case Is Pending Therein

BRIEF FOR RESPONDENTS IN OPPOSITION

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QUESTIONS PRESENTED

Whether petitioner has standing under article III of the Constitution to bring this action.

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BRIEF FOR RESPONDENTS IN OPPOSITION

I

JURISDICTION

The technical jurisdictional requirements appear to be set forth adequately in the petition except that petitioner has failed to establish its standing to sue. It also should be observed that petitioner's contentions were rejected by the United States District Court for the Northern District of California based upon and in conformity with the pertinent decisions of this Court and other federal courts. Moreover, petitioner's petition to this Court prior to briefing and decision by the Ninth Circuit Court of Ap-

peals represents nothing more than a disguised attempt by a non-United States corporation, not subject to United States jurisdiction, to have this Court legislate out of existence California's unitary method of taxation.

II

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

United States Constitution, article III, section 3 (standing of plaintiff).

III

STATEMENT OF THE CASE

A. Prefatory Statement

Petitioner has completely misstated a crucial fact in the opening sentence of its "Statement of the Case," when it states that the California State tax officials seek to assess a tax against plaintiff's subsidiary "on a portion of plaintiff's income." (Petn. for Cert., p. 3.) First, the proposed assessment was made by the Franchise Tax Board of the State of California and not by any of the named defendants. Second, the proposed assessment was an assessment against petitioner's subsidiary based on the unitary method of taxation and *not an assessment on a portion of petitioner's income.*

This misstatement vividly demonstrates the complete lack of merit in petitioner's lawsuit.

B. Relevant Facts

Petitioner EMI, Limited (hereafter "EMI") is a British corporation which owns substantially all the stock of Capitol Industries-EMI, Inc. (hereafter "Capitol"),

which is a domestic corporation doing business in California.

Franchise Tax Board (hereafter "FTB") is the agency of the State of California administering the income and franchise tax laws of that state.

The named defendants are members of the FTB and the executive officer of the FTB.

FTB assessed a tax against *Capitol, not EMI*, under the unitary method.

FTB assessed no tax, did not audit and took no action against EMI, which is outside the jurisdiction of the FTB.

On August 15, 1979, EMI and Capitol filed separate lawsuits in the United States District Court against the named defendants for injunctive and declaratory relief to enjoin the said defendants from assessing a tax against Capitol.

On February 4, 1980, the District Court ordered the lawsuits of both EMI and Capitol dismissed by granting summary judgment to the named defendants; thereafter, both EMI and Capitol appealed to the Court of Appeals, Ninth Circuit.

On February 16, 1982, the Ninth Circuit Court of Appeals remanded the two cases to the district court. (681 F.2d 1107.)

Thereupon, the district court entered an order dismissing Capitol's lawsuit in accordance with the Court of Appeal's directions. Capitol then filed a petition for certiorari (No. 82-688) with this Court, which denied it on December 13, 1982. Thus, the order dismissing Capitol's lawsuit is now final.

In the case of EMI's action, EMI filed a motion for summary judgment in July 1982.

On July 30, 1982, the named defendants filed a motion to dismiss EMI's action.

On October 8, 1982, the district court granted the named defendants' motion and ordered EMI's action dismissed.

ARGUMENT

I

EMI HAS NO STANDING UNDER ARTICLE III OF THE UNITED STATES CONSTITUTION

A. Introduction

The essence of EMI's action is found in its allegation that the named defendants have unlawfully sought to assess additional taxes against Capitol on the unitary method. EMI has no quarrel with FTB's requiring Capitol to file a combined report on a unitary basis with respect to Capitol and its United States subsidiaries. But in an effort to prevent FTB from lawfully including the unitary portion of EMI's income in the tax formula to determine the amount of Capitol's income which is properly apportionable to California under the unitary method, EMI filed the instant action for injunctive and declaratory relief prior to Capitol's exhaustion of its state administrative and judicial remedies and prior to Capitol's payment of the additional taxes assessed by the FTB.

B. The Undisputed Facts Unequivocally Demonstrate That EMI Has No Standing To Sue

On the basis of the undisputed facts, it is clear that EMI has no standing to sue. The named defendants have not assessed or sought to assess any tax against EMI, nor

have they sought to take any action against EMI, which is a foreign corporation that does no business in the United States and is not a California taxpayer. EMI is only a shareholder of Capitol, the corporation which does business in California and against which the FTB assessed a tax measured by the unitary method. Because EMI has no real basis to support its standing argument, it now finds itself relying on the speculative contention that, as a shareholder of Capitol, it will suffer the possible loss of diminished dividend income or possible diminution in the value of its shares of Capitol. The premise of these contentions is fallacious.[1]

EMI is separate and independent from Capitol, the corporation against which the FTB assessed the tax. EMI occupies the status of a shareholder of Capitol. Obviously as a shareholder, EMI has no inherent right to receive anything from Capitol. It certainly does not have the right to receive monthly, quarterly, or annual or any other form of dividend. In fact, as a shareholder of Capitol, EMI owns neither the corporate property nor the corporate earnings of Capitol; it simply has an expectancy in each. This well-established proposition was stated by the United States Supreme Court in these words:

> "The owner of the shares of stock in a company is not the owner of the corporation's property. He has a right to his share in the earnings of the corporation, as they may be declared in dividends arising from the

[1]EMI also asserts that FTB demanded information of EMI threatening it with money penalties if it did not reply. (Petn. for Cert., p. 4.) However, the Ninth Circuit Court of Appeals in the initial appeal (681 F.2d 1107, 1119) stated in footnote number 30 that the FTB had sought information from Capitol, not EMI. This fact was pointed out by Judge Samuel Conti in his order below. (See Appendix A to EMI's Petn. for Cert.)

> use of all its property. In the dissolution of the corporation he may take his proportionate share in what is left, after all the debts of the corporation have been paid and the assets are divided in accordance with the law of its creation. But he does not own the corporate property." (*Rhode Island Hospital Trust Co. v. Doughton* (1926) 270 U.S. 69, 81.)

Judge Samuel Conti expanded further on this basic legal principle in the following words in the district court below:

> "Although an injury to a corporation may indirectly harm a shareholder by decreasing the value of his shares, that fact does not give the shareholder standing to sue on his own behalf. The primary injury and the primary right to sue are the corporation's; the shareholder may sue, if at all, only in a proper derivative action. *Von Brimer v. Whirlpool Corp.*, 536 F.2d 838, 846 (9th Cir. 1976); *Erlich v. Glasner*, 418 F.2d 226, 227-28 (9th Cir. 1969); *Papilsky v. Berndt*, 466 F.2d 251, 255 (2d Cir.), *cert. denied* 409 U.S. 1077 (1972); *Jensen v. Voyles*, 393 F.2d 131, 133 (10th Cir. 1968). Therefore, EMI's claim of diminution of its investment is not sufficient to confer standing." (*EMI, Ltd. v. Bennett, et al.*, No. C-79-3146 SC (D.C.N.D. of Cal.), Oct. 8, 1982, Slip Opn. p. 2; Appendix A to EMI's instant Petn. for Cert.)

Furthermore, the threatened injury to EMI is too remote and speculative to meet standing requirements. As discussed above, EMI as a stockholder has no inherent right to receive anything from Capitol. The expectant interest which EMI has in the earnings of Capitol do not entitle it to receive monthly, quarterly, annual, or any other dividends on its stockholdings. Moreover, a corporation's declaration of dividends generally is dependent not

on earnings alone, but also on such factors as corporate expansion plans, the need to increase cash reserves and the like. Thus, whether EMI will be adversely affected by proposed tax assessments against Capitol—or benefited if such assessments are held invalid—is entirely a matter of conjecture. Even if it should be ruled that the unitary tax as applied to Capitol is unconstitutional, there is absolutely no assurance that EMI will realize any concrete benefit. At this point, there are many possibilities, but one thing is certain: it is anyone's guess whether EMI will be out-of-pocket if the assessments against Capitol are sustained by the California state courts.

Finally, there is another line of authority which holds that only a corporation, and not its stockholders, can complain of an injury or wrong done to the corporation. (*Sherman v. British Leyland Motors, Ltd.* (9th Cir. 1979) 601 F.2d 429, 439-440.) An individual stockholder, even though the sole stockholder of the corporation, cannot circumvent this rule upon the theory that he has suffered individual injury because the wrong to the corporation has adversely affected the value of his stock. (*Erlich v. Glasner* (9th Cir. 1969) 418 F.2d 266; *Gentry v. Howard* (W.D. La. 1973) 365 F.Supp. 567.) This rules applies here, where EMI is claiming potential injury from proposed California tax assessments against Capitol, its American corporate subsidiary.[3]

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[3]Stockholders have been denied relief in such actions either on the ground that they lacked "standing" or that the corporation was the "real party in interest" under rule 17(a), Federal Rules of Civil Procedure. If it is found that a stockholder complaining of injury to a corporation meets the technical requirements of standing but does not satisfy the real party in interest rule, it would appear that the prohibition contained in 28 U.S.C. section 1341

Therefore, in light of the nature of EMI's interest in Capitol, EMI cannot truly show any injury. Nor can EMI show that the relief it seeks will correct the matter. Nor is an adjudication in this case necessary because Capitol will be the best proponent of its own rights regarding the applicability to it of the unitary method of taxation. Finally, there is no obstacle to Capitol asserting its rights before the California court. Moreover, Capitol can raise in the California court all of the defenses that EMI seeks to raise here, including challenges to the constitutionality of the unitary method of taxation.

C. The Most Recent United States Supreme Court Decisions Confirm That EMI Has No Standing

In the last few years there have been several major decisions involving the question of standing. However, in none of these cases has this Court expanded the standing doctrine to a person such as EMI, which was indirectly affected by some governmental action, or where the

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could still provide a basis for dismissal of actions of this kind. For example, it is clear in the present case that Capitol has a "plain, speedy and efficient" remedy in the state courts. Hence, its joinder as the real party in interest would oust this Court of jurisdiction. Morever, the recent decisions in *Fair Assessment in Real Estate v. McNary* (1981) .... U.S. .... [70 L.Ed.2d 271], *Rosewell v. LaSalle National Bank* (1981) 450 U.S. 503, reh. den. (1981) .... U.S. .... and *California v. Grace Brethren Church* (1982) .... U.S. ...., 73 L.Ed.2d 93, emphasized the strong policy against federal interference with the fiscal operations of a state. If a state provides an adequate remedy for challenge of a tax assessment, there is no apparent reason why section 1341 should not bar a federal action by an "interested nontaxpayer" as well as the taxpayer directly concerned. It is incongruous to suggest that a state can avoid the disruptive effect of federal injunctive relief in such cases by opening up its tax proceedings to interested third parties—a cure likely to be disruptive as the ailment.

directly affected person had a remedy in the state courts, or where that person was actually litigating the identical issues against the same defendant in the state courts.

The doctrine of standing was succinctly summarized in *Simon v. Eastern Ky. Welfare Rights Org.* (1976) 426 U.S. 26 [48 L.Ed.2d 450, 96 S.Ct. 1917]. This Court stated:

> "No principle is more fundamental to the judiciary's proper role in our system of government than the constitutional limitation of federal-court jurisdiction to actual cases or controversies. See *Flast v. Cohen*, 392 U.S. 83, 95, 88 S.Ct. 1942, 1950, 20 L.Ed.2d 947, 959 (1968). The concept of standing is part of this limitation. Unlike other associated doctrines, for example, that which restrains federal courts from deciding political questions, standing 'focuses on the party seeking to get his complaint before a federal court and not on the issues he wishes to have adjudicated.' *Id.*, at 99, 88 S.Ct., at 1952, 20 L.Ed.2d at 961. As we reiterated last Term, the standing question in its Art. III aspect 'is whether the plaintiff has "alleged such a personal stake in the controversy" as to warrant *his* invocation of federal court jurisdiction and to justify exercise of the court's remedial powers on his behalf.' *Warth v. Seldin*, 422 U.S. 490, 498-49, 95 S.Ct. 219, 2205, 45 L.Ed.2d 343, 354 (1975) (emphasis in original). In sum when a plaintiff's standing is brought into issue, the relevant inquiry is whether, assuming justiciability of the claim, the plaintiff has shown an injury to himself that is likely to be redressed by a favorable decision. Absent such a showing, exercise of its power by a federal court would be gratuitous and thus inconsistent with the Art. III limitation." (426 U.S. at pp. 37-38.)

In the *Eastern Ky.* case, several indigents and organizations brought suit against the Secretary of Treasury and Internal Revenue Service Commissioner, challenging a Revenue Ruling which granted favorable tax treatment to a nonprofit hospital. This Court rejected the challenge and set forth as a standing prerequisite the need for the plaintiff to show "an injury to himself that is likely to be redressed by a favorable decision." Here not only is EMI's purported injury speculative, there is absolutely no assurance of redress. Even if this Court should rule that the unitary tax as applied to Capitol is unconstitutional, there is no assurance that Capitol will declare a larger dividend to EMI or that its value in the Capitol stock will be enhanced. Moreover, in a concurring opinion, Justice Stewart expressed the applicable maxim of tax law in the following words:

> "I add only that I cannot now imagine a case, at least outside the First Amendment area, where a person whose own tax liability was not affected ever could have standing to litigate the federal tax liability of someone else." (*Id.*, at 46.)

The *Eastern Ky.* decision was cited as controlling authority in *American Soc. of Travel Agents, Inc. v. Blumenthal* (D.C. Cir. 1977) 566 F.2d 145, cert. den. (1978) 435 U.S. 947, 98 S.Ct. 1533, where it was held that an association of travel agents and individual travel agencies had no standing to complain of the failure of federal tax authorities to assess taxes on certain income received by tax-exempt organizations, even though the organizations were in competition with plaintiffs. Similarly, in *Kent v. Northern Cal. Reg. Off. of Amer. Friends Services, Com.*

(9th Cir. 1974) 497 F.2d 1325, a group of taxpayers objecting to the federal tax on telephone services placed their tax payments into a trust pending a determination of the legality of the tax. The trustee filed an interpleader action to settle adverse claims to the fund and also sought injunctive relief. Relying on the earlier opinion in *Flast v. Cohen* (1968) 392 U.S. 83 [20 L.Ed.2d 947, 88 S.Ct. 1942], the Ninth Circuit Court of Appeals held that the trustee had standing to assert an interpleader action, but had no standing to enjoin the collection of taxes from the taxpayers themselves.

The next major standing case decided by this Court was *Duke Power Co. v. Carolina Env. Study Gp.* (1978) 438 U.S. 59, where it extended standing to an environmental organization, a labor union, and a number of residents near certain planned nuclear plants. It was not difficult for this Court to find standing in *Duke Power* because the case involved "the question of whether Congress may, consistent with the Constitution, impose a limitation on liability for nuclear accidents resulting from the operation of private nuclear power plants licensed by the Federal Government." (*Id.*, at pp. 62-63.) There is no analogy between the interests of the various plaintiffs in *Duke Power*, where the threatened nuclear injury was pervasive and compensation for damages from injury would have been unconstitutionally circumscribed, and the interest of EMI, a foreign corporation, which seeks to overthrow the sovereign taxation power of the State of California.

Duke Power was followed by *Bryant v. Yellen* (1980) 447 U.S. 352, where the United States government filed a declaratory relief action to ascertain whether section 46 of a particular law applied to leased lands. There when

the district court ruled against the United States, the latter forewent an appeal of that adverse decision. Thereupon certain persons intervened to press an appeal on their own behalf because that case was the only vehicle now available to them to have determined the question of the applicability of section 46. If section 46 applied, then the intervenors would have the possibility of purchasing certain lands. This Court extended standing to the intervenors on appeal because, if they prevailed on their contention that section 46 of the law applied, they would have the possibility of purchasing the land. On the other hand, if the adverse decision was not appealed by the intervenors in light of the United States government's failure to do so, the intervenors would never have the possibility of purchasing the land.

Obviously, the facts in *Bryant v. Yellen, id.*, are completely dissimilar from those in this lawsuit. Here Capitol is capable of asserting its legal rights in the state court. To date it has pursued every possible administrative procedure available, and if it fails in those efforts, it can pay the tax and file a suit for refund in the state court.

The next case, *Maryland v. Louisiana* (1981) ..... U.S. ..... [68 L.Ed.2d 576], is *sui generis* and clearly distinguishable. There, various states sued the State of Louisiana requesting a declaration that Louisiana's "first-use" tax was unconstitutional. This Court accepted original jurisdiction and found that the plaintiff states had standing because "The plaintiff States are substantial consumers of natural gas. . . . It is clear that the plaintiff States, as major purchasers of natural gas whose cost has increased as a direct result of Louisiana's imposition of the

First-Use Tax, are directly affected in a 'substantial and real' way so as to justify their exercise of this Court's original jurisdiction." (*Id.*, at pp. 589-590.)

This Court also went on to find a second and alternate basis for standing in these words:

> "Jurisdiction is also supported by the State's interest as *parens patriae*. A State is not permitted to enter a controversy as a nominal party in order to forward the claims of individual citizens. [Citations.] But it may act as the representative of its citizens in original actions where the injury alleged affects the general population of a State in a substantial way." (*Id.*, at 590.)

This Court then pointed out another factor favoring standing, namely, that "individual consumers . . . are foreclosed from suing for refund in Louisiana's courts." (*Id.*, at p. 591.) However, in the case of EMI, not only was the tax assessed against Capitol, the latter can still file a suit for refund in the state court. This case is similar to *Arizona v. New Mexico* (1976) 425 U.S. 794, 797, where this Court refused federal standing and held:

> "[I]n the circumstances of this case, we are persuaded that the pending state-court action provides an appropriate forum in which the *issues* tendered here may be litigated." (Emphasis in original.)

Finally, very recently in its decision in *Valley Forge College v. Americans United* (1982) ..... U.S. ..... [70 L.Ed. 2d 700], this Court reiterated the rule that "[t]he exercise of judicial power . . . is . . . restricted to litigants who can show 'injury in fact' resulting from the action which they seek to have the Court adjudicate." (*Id.*, at p. 710.) This Court also made clear that "injury in fact"

must consist of something more than the invasion of an "individuated right" or "personal constitutional right" to a governmental observance of the Constitution. Rejecting the notion that mere allegation of a legal right is sufficient to confer standing, the court stated ". . . assertion of a right to a particular kind of government conduct, which the government has violated by acting differently, cannot alone satisfy the requirements of Art. III without draining those requirements of meaning." (*Id.*, at p. 717.)

The *Valley Forge* case involved a claim by citizens and taxpayers of the United States that the government's conveyance of surplus property to a college operated by a religious order violated the Establishment Clause. Clearly, no less exacting standards for determining the standing of a litigant can apply in actions brought by a foreign corporation, such as EMI, which seeks to advance the rights of its domestic subsidiary. Here the proposed assessments to which EMI objects are directed against Capitol, which is a domestic corporation doing business in California. The FTB has no jurisdiction to assert any tax or other demands against EMI and has not done so.

Stripped down to its essentials, the complaint filed by EMI shows that it is merely a concerned bystander in a pending controversy between the FTB and Capitol. It is evident that EMI has an interest in the final outcome of that controversy. This admitted interest, however, will not suffice insofar as standing is concerned. "'[T]hat concrete adverseness which sharpens the presentation of issues,' *Baker v. Carr*, 369 U.S. [186] at 204, is the anticipated consequence of proceedings commenced by one who has

been injured in fact; it is not a permissible substitute for the showing of injury itself." (*Valley Forge College v. Americans United, supra,* 70 L.Ed.2d 718.)

No palpable "injury in fact" to EMI has been alleged in this action. Its only claim is that the proposed assessments, if allowed to stand, will result in a diminution in value of its shareholding interest in Capitol.

II

THERE IS NO EXPRESS TREATY PROHIBITION AGAINST UNITIZING FOREIGN OPERATIONS

EMI contends that the treaty provisions prohibit California from employing the unitary method to foreign unitary operations. But EMI has not pointed to any provision in any treaty that expressly prohibits such. In fact, EMI admits that the treaty upon which it apparently relies "seems not to be a model of clarity." (Petn. for Cert., p. 13.) Moreover, under the "savings" clause found in all United States tax treaties, the United States retains the right to tax its citizens, residents and corporations on the basis of their worldwide income as though the treaty had not come into effect.

III

CALIFORNIA COURTS CAN AND ARE FULLY QUALIFIED TO DECIDE THE QUESTION OF THE CONSTITUTIONALITY OF THE UNITARY METHOD OF TAXATION AS APPLIED TO EMI'S UNITED STATES SUBSIDIARY

Even in this age of profligate lawsuits, this action by EMI is incredible. This is not an action involving any basic inalienable constitutional rights of a resident or citizen of the United States. Quite to the contrary. This is an

action by a foreign corporation, which is not even subject to California jurisdiction, seeking to utilize the Federal courts to judicially overthrow the sovereign taxation powers of the State of California.

If California's unitary method is as unconstitutional and illegal as EMI would have this Court believe, the California appellate and supreme courts would nullify it. After all, EMI has not furnished any evidence that the California courts are not capable of understanding the law. Nor is there any evidence that the California courts would not follow the laws as interpreted by the United States Supreme Court. Moreover, if Capitol does not have enough conviction to pursue its own direct rights in a lawsuit in the courts of the State of California, what reason is there for its shareholder, EMI, to pursue an action in the federal court in support of a speculative and indirect right?

EMI's suit is also disruptive of the entire judicial process. There are recognized principles and procedures governing challenges to state taxes. In addition, there is the proscription against multiple lawsuits. In this day when the public is clamoring for less taxes and greater government efficiency, responsible persons should seek to minimize litigation. This lawsuit completely violates these principles. There is not one valid reason for a nontaxpayer such as EMI to challenge a state tax imposed on its subsidiary when the latter has an adequate and speedy remedy in the California courts. (*Aronoff v. Franchise Tax Board* (1965) 348 F.2d 9.) Moreover, there will be utter chaos if every disgruntled taxpayer sought to attack various state tax laws in the federal courts under the guise of some purported violation of sundry provisions of the constitution.

CONCLUSION

In summary, EMI has totally failed to establish that it has standing to sue. EMI also has not pointed to the existence of a single fact, as opposed to its conjective and speculative assertions, to demonstrate that the named defendants have violated EMI's purported rights under the United States Constitution or laws. Nor has EMI cited one case which supports its contention that the FTB cannot assess a corporation doing business in California, viz., Capitol, under the unitary method. Thus, EMI's action is totally devoid of merit, and the petition should be denied.

Dated: January 12, 1983

Respectfully submitted,

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